

Saudi Fund Road Network Development Project - 2015

The audit of financial statements of the Saudi Funded Road Network Development Project for the year ended 31 December 2015 was carried out under my direction in pursuance of provisions in Article 154(1) of the Constitution of the Democratic Socialist Republic of Sri Lanka read in conjunction with Loan Agreement No. 9/574 dated 30 October 2012 entered into between the Democratic Socialist Republic of Sri Lanka and the Saudi Fund for Development.

1.2 Implementation, Objectives, Funding and Duration of the Project

According to the Loan Agreement of the Project, then the Ministry Highways Port and Shipping, presently the Ministry of Higher Education and Highways is the Executing Agency and the Road Development Authority is the Implementing Agency of the Project. The objective of the Project is to rehabilitate and improve 138.39 kilometres of the sections of 09 roads in the Central, Eastern, Sabaragamuwa, Western and North Western Provinces. As per the Loan Agreement, the estimated total cost of the Project amounted to US\$ 81.75 million equivalent to Rs.10,628 million and out of that US\$ 60 million equivalent to Rs.7,800 million was agreed to be provided by the Saudi Fund for Development. The Project commenced its activities on 03 June 2013 and scheduled to be completed by 31 December 2016.

1.3 Responsibility of the Management for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with Sri Lanka Public Sector Accounting Standards and for such internal control as the management determines is necessary to enable the preparation of financial statements that are free from material misstatements, whether due to fraud or error.

1.4 Auditor's Responsibility

My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with Sri Lanka Auditing Standards. Those Standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatements. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risk of material misstatements of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Project's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Project's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the management as well as evaluating the overall presentation of the financial statements. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my opinion. The examination also included such tests as deemed necessary to assess the following.

- (a) Whether the systems and controls were adequate from the point of view of internal control so as to ensure a satisfactory control over Project management and the reliability of books, records, etc. relating to the operations of the Project.

- (b) Whether the expenditure shown in the financial statements of the Project had been satisfactorily reconciled with the enhanced financial reports and progress reports maintained by the Project.
- (c) Whether adequate accounting records were maintained on a continuing basis to show the expenditure of the Project from the funds of the Government of Sri Lanka and the Lending Agency, the progress of the Project in financial and physical terms, the assets and liabilities arising from the operations of the Project, the identifications of the purchases made out of the Loan, etc.
- (d) Whether the withdrawals under the Loan had been made in accordance with the specifications laid down in the Loan Agreement.
- (e) Whether the funds, materials and equipment supplied under the Loan had been utilized for the purposes of the Project.
- (f) Whether the expenditure had been correctly identified according to the classification adopted for the implementation of the Project.
- (g) Whether the financial statements had been prepared on the basis of Sri Lanka Public Sector Accounting Standards.
- (h) Whether satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (i) Whether the financial covenants laid down in the Loan Agreement had been complied with.

2. Financial Statements

2.1 Opinion

So far as appears from my examination and to the best of information and according to the explanations given to me, I am of opinion that,

- (a) the Project had maintained proper accounting records for the year ended 31 December 2015 and the financial statements give a true and fair view of the state of affairs of the Project as at 31 December 2015 in accordance with Sri Lanka Public Sector Accounting Standards,
- (b) the funds provided had been utilized for the purposes for which they were provided,
- (c) the satisfactory measures had been taken by the management to rectify the issues highlighted in my previous year audit report, and
- (d) the financial covenants laid down in the Loan Agreement had been complied with.

3. Financial and Physical Performance

3.1 Utilization of Funds

Certain significant statistics relating to the financing, budgetary provision for the year under review and the utilization of funds during the year under review and up to 31 December 2015 are shown below.

| Source | Amount agreed for financing in the Loan Agreement | | Allocation made in the Budget Estimate for the year under review | <u>Funds utilized</u> | | | |
|----------------------------|---|----------------------|--|-----------------------|------------------------|---------------------|------------------------|
| | US\$ million | Rs. million | | US\$ million | Rs. million | US\$ million | Rs. million |
| Saudi Fund for Development | 60.00 | 7,800 | 3,805.00 | 21.77 | 2,944.61 | 37.10 | 4,937.70 |
| GOSL | 21.75 | 2,828 | 72.39 | - | 56.22 | - | 176.50 |
| | ----- | ----- | ----- | ----- | ----- | ----- | ----- |
| | <u>81.75</u> | <u>10,628</u> | <u>3,877.39</u> | <u>21.77</u> | <u>3,000.83</u> | <u>37.10</u> | <u>5,114.20</u> |

According to the above information, only US\$ 37.10 million equivalent to Rs. 4,937.70 million representing 61.83 per cent had been utilized up to 31 December 2015, out of the total allocation of US\$ 60 million equivalent to Rs. 7,800 million made for the Project. Thus it indicated that the use of balance allocation of US\$ 22.90 million during the remaining period of 01 year of the Project was very remote.

3.2 Physical Progress

According to the progress reports of the Project, rehabilitation and improvement works of 50 kilometres of 03 sections of Kandy – Jaffna Road from Katugastota to Naula, 7.24 kilometres of Colombo-Kandy Road from Peliyagoda to Kiribathgoda and 8.5 kilometres of Thampalagamam-Kinniya Road had been completed by the Project and handed over to the Road Development Authority as at 31 December 2015. Further, the rehabilitation and improvement works of 14 kilometres of Dehiowita- Deraniyagala Noori Road had been substantially completed as at 31 December 2015.

3.3 Contract Administration

The following observations were made.

- (a) It was observed that the approach roads to the District Hospital, Divisional Secretariat Office and the Police Station of Deraniyagala had also been improved by the Project even though such activities were not included in the scope of the works for the rehabilitation and improvements of Dehiowita- Deraniyagala Road. As a result, a cost overrun amounting to of Rs.161.52 million had been approved by the Project through 27 variation orders. It was observed in audit that the additional costs incurred thereon could have been minimized if the Project Monitoring Unit had taken action to carry out proper detailed designs of the rehabilitation works at the initial stages.

- (b) The site inspections made by the auditors on 11 July 2016 had revealed several defects in the road surface of 11 kilometres of the section from Katugastota to Alawatugoda of Kandy – Jaffna Road as described below.

| Nature of the defects | No. of instances observed metres |
|------------------------------|---|
| ----- | ----- |
| Cracks in the road surface | 221 |
| Damages of the road surface | 56 |
| Road shoulder slipped away | <u>146</u> |
| Total defects | <u>423</u> |

Further, 04 instance of damages of road surface and 28 liner metres slipped away of the shoulders of 17 kilometres of the road section from Alawatugoda to Palapathwela of Kandy-Jaffna Road had also been investigated at the time of site investigation made by the auditors.

3.4 Transactions with Contentious Nature

It was observed that the contractor engaged for the rehabilitation and improvement works of the section of Kandy – Jaffna Road from Katugastota to Alawatugoda had been paid a sum of Rs.3.58 million additionally as an interest on settling claims with delays.